Federal Reserve Governor Jerome Powell said regulators are developing the tools needed to dismantle large and failing financial institutions to help remove the benefit from being seen as too big to fail.

“Today, the market still appears to provide a subsidy, of changing and uncertain amount, to very large banks to account for the possibility of a government bailout in the event of failure,” Powell said today in a speech in Washington. “The market needs to believe -- and it needs to be the case -- that every private financial institution can fail and be resolved under our laws without imposing undue costs on society.”

Proposed regulations are “designed to accomplish just that,” Powell said at an Institute of International Bankers conference, citing efforts initially to implement stronger capital and liquidity rules and then to create a liquidation authority to resolve a failing bank.

Lawmakers and regulators, including the Fed, are pushing to limit the risk that the government will need to rescue a big U.S. bank. Fed Governor Daniel Tarullo, Dallas Fed President Richard Fisher and Senator Sherrod Brown, an Ohio Democrat, are among the policy makers and legislators who have said the 2010 Dodd-Frank act overhauling financial regulation failed to curb the growth of large lenders and protect taxpayers against bailouts.

“My own view is that the framework of current reforms is promising and should be given time to work,” Powell said. “In any case, too-big-to-fail must end, even if more intrusive measures prove necessary in the end.”

Yield Rises

The Standard & Poor’s 500 Index was little changed at 1,518.96 at 1:46 p.m. in New York, while the yield on the 10- year Treasury note climbed 0.03 percentage point to 1.87 percent.

Regulators and lawmakers from both parties raised concerns at a Feb. 14 Senate Banking

Committee hearing about whether the government will have to step in to rescue firms whose collapse would threaten the broader economy. Senator Elizabeth Warren, a Massachusetts Democrat, said the number of prosecutions of executives after the 2008 financial crisis was inadequate and suggested that regulators consider Wall Street "too big for trial."

Powell said in response to audience questions that creditors and managers of a failing bank would suffer under the new resolution regime.

'Wiped Out'

"We're envisioning a world in which the equity is wiped out, the creditors bear losses, the senior management bears the loss of their job and quite possibly a lot else," Powell said. "At that point, you've eliminated any moral hazard that might exist."

Fed Chairman Ben S. Bernanke, at a Feb. 26 banking committee hearing, was pressed to curb too-big-to-fail banks by Warren and David Vitter, a Republican from Louisiana.

"We've now understood this problem for nearly five years, so when are we going to get rid of too big to fail?" Warren said to Bernanke.

The central bank is putting "a lot of effort into this," Bernanke said. "As somebody who has spent a lot of late nights trying to deal with these problems during the crisis, I would very much like to have the confidence that we could close down a large institution without causing damage to the rest of the economy," he said.

More Capital

Strategies under consideration range from legislation that would cap the size of big banks or make them raise more capital, to regulatory actions to discourage mergers or require that financial firms hold specified levels of long-term debt to convert into equity in a failure.

Powell said that if the current measures “achieve their purpose, in my view they would be preferable to a government- imposed break-up, which would likely involve arbitrary judgments, efficiency losses and a difficult transition.”

Lawmakers from both political parties have expressed support for renewed efforts to limit the kind of systemic risk that fueled the 2008 financial crisis. **Representative John Campbell**, **a Republican from California, said Feb. 11 he plans to offer legislation intended to shrink too-big-to-fail banks by requiring them to hold more capital, including long-term debt.**